



American Revolution Bicentennial

FEDERAL RESERVE BANK OF DALLAS

DALLAS, TEXAS 75222

Circular No. 76-30

March 2, 1976

INTERPRETATION OF REGULATIONS K, M, AND Y

Statement of Policy on Stock Interests in Foreign Joint Ventures

TO ALL BANKS, BANK HOLDING COMPANIES,
AND OTHERS CONCERNED IN THE
ELEVENTH FEDERAL RESERVE DISTRICT:

On February 12, 1976, the Board of Governors of the Federal Reserve System issued an interpretation to its Regulation K, "Corporations Engaged in Foreign Banking and Financing Under the Federal Reserve Act," Regulation M, "Foreign Activities of National Banks," and Regulation Y, "Bank Holding Companies," stating its policy on the acquisition of stock interests in foreign joint ventures by U.S. banking organizations. The policy is designed to deal with possible future risks entailed in becoming a shareholder in a foreign joint venture.

As a matter of policy, the Board will take the following factors, among others, into account in considering whether to approve an application to invest in a foreign joint venture:

- (1) The possibility that the venture might need additional financial support, and
- (2) The possibility that the additional support might be significantly larger than the original equity investment in the joint venture.

The policy statement is not intended to prohibit or discourage joint ventures abroad. Its objective is to clarify for all parties the probable dimensions of the risks involved in such ventures.

Enclosed is a copy of the interpretation. Inquiries regarding the matter should be directed to our Regulations Department at (214) 651-6325. Additional copies of this interpretation will be furnished upon request to the Secretary's Office of this Bank.

Sincerely yours,
T. W. Plant
First Vice President

Enclosure

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

CORPORATIONS ENGAGED IN FOREIGN BANKING AND
FINANCING UNDER THE FEDERAL RESERVE ACT
FOREIGN ACTIVITIES OF NATIONAL BANKS

BANK HOLDING COMPANIES

INTERPRETATION OF REGULATIONS K, M, AND Y

SECTION 211.52 — STATEMENT OF
POLICY ON STOCK INTERESTS IN
FOREIGN JOINT VENTURES*

In general, when a member bank or a corporation organized under § 25(a) of the Federal Reserve Act (an "Edge" corporation), or operating pursuant to an agreement with the Board under § 25 thereof (an "Agreement" corporation), or a bank holding company requests the Board's specific consent to acquire the stock or other certificates of ownership of a foreign corporation that will be jointly-owned by the U.S. banking organization and other foreign or domestic participants (hereinafter referred to as a "foreign joint venture"¹), the Board considers, among other factors, the degree of legal and practical business responsibility the U.S. banking organization will bear for the financial condition and operations of the foreign joint venture in foreign and international financial markets. In the Board's judgment, this factor, among others, is relevant in assessing what effects the proposed investment may have on the financial and managerial resources of the applying U.S. banking organization.

Based on the recent experience of certain foreign joint ventures in foreign and international financial markets, the Board has found that a U.S. banking organization may, in certain circum-

stances, feel impelled for business reasons to provide financial support² to a foreign joint venture in which it has an equity interest in the event the venture has liquidity or other financial needs. This support may be substantially in excess of the U.S. banking organization's original equity investment and may, in some situations, be well in excess of its *pro rata* share. This has seemed most likely to occur in situations where (1) the foreign joint venture has included in its name a reference to the U.S. banking organization, (2) the U.S. banking organization or its affiliates have consistently provided financial support to the foreign corporation in amounts significantly beyond usual commercial limits or significantly disproportionate to its *pro rata* stock interest, or (3) as the result of substantial managerial support furnished by the U.S. banking organization under a contract or other arrangement, the foreign corporation has been publicly identified as or considered to be, sometimes with the active encouragement of the U.S. banking organization, an integral part of the U.S. banking organization's international operations.

Accordingly, the Board, in considering applications by U.S. banking organizations to invest in foreign joint ventures, will, as a matter of policy, take into account the possibility that the applicant may feel impelled for business reasons to provide

*This interpretation is also indexed as sections 213.52 and 225.51.

¹ The term "foreign joint venture" is used to describe a situation in which a U.S. banking organization with a minority share interest participates, directly or indirectly, in the overall management of the corporation and thus has an active operating interest. A purely passive minority investment in a foreign corporation will not be deemed a "joint venture" investment for purposes of this statement of policy. This "joint venture" determination will be made on the basis of the facts and circumstances of each case.

² As used herein, the term "support" includes, without limitation, contributions to capital, purchase (or causing the purchase) from the foreign corporation of loans or securities, making (or causing the making) of loans to the foreign corporation, and the making (or causing the making) of deposits in the foreign corporation.

financial support for such foreign joint venture in the event the venture has liquidity or other financial needs, and that such support could be significantly greater than the amount of its proposed equity investment. The Board will, therefore, consider such application in light of the relative ability of the applicant to meet the demands that such potential support could place on its financial and managerial resources. In doing so, the Board will take into consideration the risks associated with the total assets and liabilities of the foreign venture and its projected expansion, and not merely the size of the proposed equity investment by the applicant. In particular, the Board will give great weight to these potential risks and their implications for the applicant in cases where the applicant proposes (1) to include a reference to its name in that of the foreign joint venture, (2) to provide general funding support to the foreign joint venture in amounts disproportionate to its *pro rata* stock interest, or (3) to provide virtually all of the management for such foreign joint venture.

If, however, in the case of any such proposed joint venture investment, the U.S. banking organization can establish in the record of its application that it has reached an agreement or arrangement whereby its support of the proposed joint venture in the event of liquidity or other financial needs will be limited to its initial equity investment or to some fixed amount, or will be shared *pro rata* or otherwise with the other shareholders, or will otherwise be limited, the Board will consider the application and the risks associated therewith on the basis of this additional information. In this regard, the Board will also consider the identity and financial strength of other partners and investors in the venture and their respective ability to provide support to the venture, if needed.

This statement of policy is not intended to prohibit or discourage investments by U.S. banking organizations in foreign joint ventures, which can be a useful form of corporate organization in

appropriate circumstances; rather, due to the difficulty of ascertaining the precise risks undertaken in joint venture investments, its primary purpose is to clarify for all parties concerned the probable dimensions of risks assumed in any particular investment. Thus, even if an applicant proposes to assume a disproportionate share of the risks in any joint venture, e.g., agrees to stand behind more than its *pro rata* share of the joint venture's obligations, the Board might be willing to approve the investment if the applicant's financial and managerial resources could bear this additional risk and if other factors indicated that approval would be consistent with the public interest.

The Board further notes that any action that it might take on an application should not be viewed or relied upon by the applying U.S. banking organization, other participants in the venture, or any third party as constituting approval or disapproval, or ratification or rejection of any agreement or arrangement that may have been entered into by the shareholders of a foreign joint venture; specifically, any Board action should not be viewed as constituting any expression of judgment as to the validity or enforceability of any such agreement or arrangement. Any agreement or arrangement will, rather, be merely one among many factors considered by the Board in deciding on an application.

This statement is intended to apply primarily to proposed investments by U.S. banking organizations in the stock of foreign corporations in which they do not already have an equity investment. Applications involving an additional investment in an ongoing foreign joint venture will continue to be considered by the Board on the basis of outstanding facts and circumstances. In the case of any ongoing foreign joint venture the Board will, of course, continue to consider carefully the amount of support, if any, that is being provided by the applicant to the venture and any agreement or arrangement among the joint venturers for the provision of any future support.